

Sellers of special order machines are considered to be engaged primarily in a service occupation, rather than being engaged in the business of selling tangible personal property, if the test set out in 86 Ill. Adm. Code 130.2115(b) is met. See 86 Ill. Adm. Code 130.2115. (This is a GIL.)

April 14, 2006

Dear Xxxxx:

This letter is in response to your letter dated March 29, 2005, in which you request information. We apologize for our delay in responding to you. The Department issues two types of letter rulings. Private Letter Rulings ("PLRs") are issued by the Department in response to specific taxpayer inquiries concerning the application of a tax statute or rule to a particular fact situation. A PLR is binding on the Department, but only as to the taxpayer who is the subject of the request for ruling and only to the extent the facts recited in the PLR are correct and complete. Persons seeking PLRs must comply with the procedures for PLRs found in the Department's regulations at 2 Ill. Adm. Code 1200.110. The purpose of a General Information Letter ("GIL") is to direct taxpayers to Department regulations or other sources of information regarding the topic about which they have inquired. A GIL is not a statement of Department policy and is not binding on the Department. See 2 Ill. Adm. Code 1200.120. You may access our website at www.ILTAX.com to review regulations, letter rulings and other types of information relevant to your inquiry.

The nature of your inquiry and the information you have provided require that we respond with a GIL. In your letter you have stated and made inquiry as follows:

ABC requests a private letter ruling on the tax applicable to the equipment and services that we provide. There is no litigation or audit pending with the department, and ABC has not previously requested nor has the department previously ruled on the same or similar issue for ABC. There are no statements of authorities that have been located either supporting or contrary to ABC views. ABC is making an effort to operate a business in the state of Illinois within the rules and regulation and has not been able to find any clearly defined statutes addressing its business type.

ABC is a materials handling systems integrator. These turnkey systems may include mechanical equipment (conveyors, mezzanines, pallet rack, etc.), controls engineering and equipment, project management, and/or installation services. To assist in your decision, a detailed description of the sales process as well as the services and equipment provided follows.

- ? During the concept and layout design, we evaluate the customer's material handling needs and provide a proposal and layout drawing. This requires **travel and engineering time** that becomes part of project management/engineering, which may be separately stated in customer pricing.

- ? If we receive an order, additional **engineering and design time** is expended to provide detailed drawings, which clearly defines the equipment to be placed on order and the field installation of the equipment at the customer's facility.
- ? ABC considers the **mechanical equipment** that we sell to be tangible personal property. We do not manufacture the mechanical equipment in house. We place orders with various dealers' factories that can provide equipment that is most appropriate for the system. As a rule, the equipment is shipped directly from the factories to the customer's facility.
- ? If the system includes **electrical controls**, this portion of the system may be subcontracted or provided by ABC's electrical controls department. If it is subcontracted, the electrical controls are normally purchased as a subsystem. If ABC electrical controls department is used to provide this aspect of the contract, we will provide **design engineering**, along with a combination of supplying the **computer hardware, software, and programming**. We will also **fabricate the control panel**, which is a combination of controls equipment in a metal enclosure. The pricing on the electrical controls portion may be broken out any number of ways including: 'Controls and Software', 'Controls and Programming', 'Controls Equipment' and 'Controls Engineering' separately, or as 'Electrical Controls' as a single item.
- ? **Installation services** (mechanical and electrical) are usually sold as part of the contract; however, it is possible for the customer to assume responsibility for this portion of the system. ABC subcontracts all installation services.
- ? **Project management services** are provided by ABC, from our **office** to coordinate all aspects of the system from quotation to completion and at the **jobsite** to make sure that the installers adhere to schedule and specifications and ensure the customer's satisfaction. The initial **engineering and design services** may be consolidated into this portion of the contract.
- ? A ABC **project manager** and other ABC personnel will be on site for system start-up to run-in and de-bug as well as to perform other functions that are an integral part of providing a turnkey material handling system.

The relative value of equipment, engineering, and installation varies on each project, with the following approximate ranges: equipment---40% to 70%, installation---20% to 40%, engineering---7% to 20%.

ABC is committed to complying with the statutes of the state of Illinois. Your prompt attention to this matter is greatly appreciated.

If you require further clarification of any of the statements made in this writing, please feel free to contact me.

DEPARTMENT'S RESPONSE

Without a review of the specific contractual agreements with your company's clients, we cannot provide you with a Private Letter Ruling. However, we hope the following information will be helpful.

Based upon the information you have provided, we suggest you refer to the Department's regulation regarding Sellers of Machinery, Tools and Special Order Items. 86 Ill. Adm. Code 130.2115. This will help you determine whether your business is subject to Retailers' Occupation Tax or Service Occupation Tax. If your business meets the test set out in Subsection 130.2115(b), it will

be subject to Service Occupation Tax rather than Retailers' Occupation Tax. A brief summary of the Service Occupation Tax follows.

The purchase of tangible personal property that is transferred to service customers may result in either Service Occupation Tax liability or Use Tax liability for the servicemen, depending upon how the serviceman calculates his or her liability. There are four ways that the tax can be calculated: (1) separately stated selling price; (2) 50% of the entire bill; (3) Service Occupation Tax on the cost price if they are registered de minimis servicemen; or, (4) Use Tax on the cost price if the servicemen are de minimis and are not otherwise required to be registered under Section 2a of the Retailers' Occupation Tax Act.

Using the first method, servicemen may separately state the selling price of each item transferred as a result of sales of service. The tax is based on the separately stated selling price of the tangible personal property transferred. If servicemen do not wish to separately state the selling price of the tangible personal property transferred, those servicemen must use the second method where they will use 50% of the entire bill to their service customers as the tax base. Both of the above methods provide that in no event may the tax base be less than the cost price of the tangible personal property transferred. Under these methods, servicemen may provide their suppliers with Certificates of Resale when purchasing the tangible personal property to be transferred as a part of the sales of service. Upon selling their product, they are required to collect the corresponding Service Use Tax from their customers. See 86 Ill. Adm. Code 140.106.

The third way servicemen may account for their tax liability only applies to de minimis servicemen who have either chosen to be registered or are required to be registered because they incur Retailers' Occupation Tax liability with respect to a portion of their business. Servicemen may qualify as de minimis if they determine that their annual aggregate cost price of tangible personal property transferred incident to sales of service is less than 35% of their annual gross receipts from service transactions (75% in the case of pharmacists and persons engaged in graphic arts production). See 86 Ill. Adm. Code 140.101(f). This class of registered de minimis servicemen are authorized to pay Service Occupation Tax (which includes local taxes) based upon the cost price of tangible personal property transferred incident to sales of service. Servicemen that incur Service Occupation Tax collect the Service Use Tax from their customers. They remit the tax to the Department by filing returns and do not pay tax to suppliers. They provide suppliers with Certificates of Resale for the property transferred to service customers. See 86 Ill. Adm. Code 140.108.

The final method of determining tax liability may be used by de minimis servicemen not otherwise required to be registered under Section 2a of the Retailers' Occupation Tax Act. Servicemen may qualify as de minimis if they determine that their annual aggregate cost price of tangible personal property transferred incident to sales of service is less than 35% of their annual gross receipts from service transactions (75% in the case of pharmacists and persons engaged in graphic arts production). Such de minimis servicemen may pay Use Tax to their suppliers or may self assess and remit Use Tax to the Department when making purchases from unregistered out-of-State suppliers. Those servicemen are not authorized to collect "tax" from their service customers because they, not their customers, incur the tax liability. Those servicemen are also not liable for Service Occupation Tax. It should be noted that servicemen no longer have the option of determining whether they are de minimis using a transaction-by-transaction basis. See 86 Ill. Adm. Code 140.109.

I hope this information is helpful. If you require additional information, please visit our website at www.ILTAX.com or contact the Department's Taxpayer Information Division at (217) 782-3336. If you are not under audit and you wish to obtain a binding PLR regarding your factual situation, please submit a request conforming to the requirements of 2 Ill. Adm. Code 1200.110 (b).

Very truly yours,

Martha P. Mote
Associate Counsel

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